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Economic Conditions Governmental Finance United States Securities

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General Business Conditions

THE developments in trade and industry during the past month have been generally of an encouraging character. When the upturn in the markets occurred in June it took most people by surprise, and business men, while welcoming the change, have hesitated to draw conclusions from it that seemed too good to be true. However, as the first signs of improvement have multiplied and business has held and extended its gains, the feeling has grown that the worst has been seen and that the country is headed for some measure of recovery.

Despite its rapid advance in June, the stock market in July not only has stubbornly refused to conform to the popular expectation of reaction, but has even moved into new high ground. The rise in the market has been an event of outstanding importance, spreading hope and encouragement throughout all business. Of course, it would be incorrect to attribute the improvement in business primarily to the rise of security prices; the sequence is rather the other way around. Nevertheless, the stock market has provided a visible symbol of an improvement which to many people had gone unnoticed. Hence its rise has had a cheering effect that has stimulated buying and given cumulative force to other influences making for betterment.

The fact is that business reports early in June began to give evidence that deflationary tendencies were encountering increasing resistance. The decline in commodity prices had halted around the first of the month, and weekly indexes of business activity, which had been falling almost uninterruptedly since last September, flattened out and in some instances commenced to show a recovery. It will be admitted that gains over so short a period can hardly be considered conclusive; nevertheless, the vigor of the rise in the security markets, and the spirited character of the buying in numerous commodity lines, have been impressive, especially when consideration is given to the drastic restrictions placed upon production during the past nine months and the prospect of vastly increased expenditures by the Government over the coming year.

For approximately a year, business has been engaged in an effort to reduce inventories built up in 1936 and the early part of 1937, and production in practically all lines was cut below consumption. Sooner or later such movements bring their own cure at the point where surplus stocks are exhausted, and buying and production have to be increased to take care of current needs. This is the way that depressions have ended in the past, and is probably as good an explanation as any of the developments of the past two months. While visible stocks of primary commodities have remained large, information has been to the effect that stocks of manufactured goods were being steadily reduced, especially in wholesale and retail channels, and recent events have tended to confirm these impressions. Business men were prepared to see trade and production go to still lower levels during the Summer, and with indications that Summer business might be better than expected, became nervous as to nearby requirements and rushed to cover. Once business men become convinced that a bottom has been reached the psychology quickly changes and everyone wants to buy at once.

Consumer Goods Industries Leading

In the recovery from previous depressions, the consumer goods industries have usually shown the way, and happenings of recent weeks suggest that this experience is being repeated. This was true in 1933 and there is logical basis for it in the fact that this class of goods is by and large of relatively short life and needs to be replaced at frequent intervals. Sentiment throughout these industries has undergone a marked change for the better since the early part of June, and the volume of business done has been the most satisfactory since the onset of the depression. Buying for the Fall retail season, which commences in July, has started off in good fashion. Retailers, having enjoyed an improvement in business, and sensing a

generally better feeling, have revised their budgets upward, but are buying conservatively, content to rely on reorders if conditions warrant. This is a healthy attitude and should lessen the chances of reactions.

Evidence of the improvement in retail distribution has appeared in nationwide reports. While sales of leading merchandising organizations continue to run below the corresponding figures a year ago, the spread in most cases has narrowed. Thus, dollar totals for department stores reporting to the Federal Reserve Board for the first two weeks of July were 6 and 8 per cent, respectively, under those a year ago, compared with losses of 13 to 19 per cent during May and early June. Chain store sales reflect a similar trend, and mail order houses are feeling a pickup; in June Montgomery Ward sales were down only 3.5 per cent from last year, as against 7.6 per cent in May, while sales of Sears, Roebuck & Co., though off more than those of its big competitor, were better relatively than in the previous four weeks. Taking account of the lower prices, it appears that the actual quantity of merchandise distributed is running close, if not equal, to that of a year ago. Stocks of goods in retail hands have diminished, and for reporting department stores were 12 per cent less in dollar value at the end of June than on the corresponding date last year.

Cotton mills did a big business during the latter part of June and fore part of July, sales for several weeks running well in excess of production, but lately trading has slackened off. Buyers, having filled nearby requirements, are disposed to await developments before making additional commitments. Thanks to the big volume booked, mill stocks, which had been uncomfortably large, have been reduced, and mill margins somewhat improved. Production is increasing. Business in other lines has broadened encouragingly, with prices showing a firmer trend. Wool prices are higher, and woolen goods are being advanced along with expanding mill activity. Heavy purchases of surplus clothing stocks by the Government have lifted operations in the men's clothing field. Silks and rayon are more active and firm, while substantial trade orders for Fall shoes have strengthened hides and leathers and brightened the manufacturing outlook. Attendance at mid-Summer furniture and house furnishings shows has been good and results gratifying.

Steel and Automobiles Do Better

Perhaps the most significant improvement has been in the steel and automobile industries, both of which have been turning in a better Summer performance than had been looked for. Weekly production at the steel plants, which had eased in May and early June to 26 per cent of capacity, rose by the latter part of July to 37 per cent, the best showing for the year to date. An upturn in steel production at this season is unusual and indicates the general depletion of the inventories of consuming industries. Notwithstanding the price cuts of a month ago, forward buying does not appear to have increased much, and considerable confusion exists as to the ultimate effects of the change in prices and pricing methods. Due, however, to necessitous demand, steel makers expect mill operations to advance during coming months, and the firmness of steel scrap supports this view, but anything like full activity can hardly be looked for without a revival in the heavy industries.

The problem of costs remains a difficult one for the steel industry, as for industry generally. The reduction of steel prices inevitably raises a question as to steel wage rates, now the highest in the history of the industry and approximately 28 per cent above 1929. Thus far in 1938 most of the companies are in the "red" and manifestly the lower prices, unless accompanied by a lowering of costs through substantially increased volume or otherwise, will only involve them in heavier losses. Producers have insisted that prices could not be cut without affecting wages, but evidently are disposed to give the situation a trial. One thing is certain, — the companies cannot go on indefinitely operating at a loss.

In the motor industry, an improvement in retail sales has maintained the production of 1938 models longer than had been anticipated. Whereas factory schedules at the outset of June called for assemblies of approximately 155,000 units, (United States and Canada), actually the month turned out nearer to 190,000. Moreover, July retail sales, contrary to precedent, are reported to have approximated those of June, while assemblies for the week of July 16th were the largest since May, albeit much below those of the corresponding week last year. For some time the production of new cars has been held below deliveries, resulting in a steady reduction of dealers' stocks. Also, the troublesome used car situation is said to be definitely clearing. While production from now on is expected to taper off in anticipation of model changes, the industry should go into the new season in good shape to benefit from any improvement in general conditions. Few industries respond more promptly to a change in psychology than does the motor industry; and obviously an upturn in this quarter would have broadly stimulating results, both by providing more jobs and through increased requirements for steel and other materials.

The value of construction contracts awarded in June, reported by the F. W. Dodge Corporation, was 21 per cent below that of June a year ago, and the first half of July showed a drop of 32 per cent. A feature of the

building reports has been the improvement in the residential classification since the early months of the year. After starting 1938 with a drop of 55 per cent (January) below corresponding totals in 1937, the comparisons improved until in May residential contract awards were nearly even with those of last year. For June the figures dropped back moderately, but the first two weeks of July have turned in an increase of 1.7 per cent. A hopeful feature in the building outlook has been the success of the Federal Housing Administration in stimulating residential construction, especially in the small home field, by a reduction of financing costs, plus certain economies resulting from large-scale operations. In the four months since February, when the amended F.H.A. program went into effective operation, to July 1, mortgages selected by the F.H.A. for appraisal totaled $382,000,000, an increase of 53 per cent over the $249,000,000 selected for the corresponding months of 1937. It is of interest that in 1937 almost half of the borrowers under the F.H.A. program had incomes under $2,500 annually, and one-quarter of them had incomes from $2,500 to $3,500.

Other Indications of Improvement

Replacement tire sales have held up well and with manufacturers' stocks reduced in line with current shipments, production of tires is expected to expand moderately in the third quarter. Rubber consumption in the second quarter rose slightly above the first quarter levels, but for the first half year was the smallest for any corresponding period since 1923. Further expansion is looked for in the third quarter and with production drastically curtailed and world stocks now declining, rubber prices have had a sharp rise to 16 cents from 11 cents late in April.

Non-ferrous metals came in for heavy buying in June and early July, and prices were marked up all along the line. Domestic copper sales in June, amounting to 87,843 tons, were the largest since 1936, and sales in July were even larger. Thanks partly to the heavy sales and partly to earlier severe restrictions on production, the non-ferrous metals give first indications of having turned the corner. Thus, the long sharp rise of stocks in producers' hands was halted during June, and both copper and lead stocks at the end of the month were smaller, and zinc stocks only slightly larger, than at the beginning.

Mention is in order also of a small, but encouraging, rise of machine tool orders during June. Demand for building materials, including lumber, cement and brick, has picked up, along with improved sentiment as to general business and building prospects. Movement of traffic over the railways, as measured by car loadings, has gained in recent weeks, seasonal changes allowed for, and in the week of July 16 showed the smallest drop from a year ago, 21.4 per cent, since February.

The Basis of Prosperity

The foregoing review of business trends presents a welcome contrast to the procession of gloomy statistics that has come forward up to this time. Evidently the slowing down of normal business operations has been too drastic, and the needs of the country for goods and services are again asserting themselves. In every depression the tendency is for production to decline more than consumption while accumulated stocks are being worked off, and apparently the experience of the past year has been no exception. From the high point of activity reached in the Spring of 1937, industrial production, as measured by the Federal Reserve Board's monthly index, has fallen approximately 35 per cent, a decline of unprecedented magnitude for so short a period. At the same time the great body of consumer incomes available for spending has undergone no such shrinkage. Although wages have been lost by reason of unemployment, and dividends reduced, the buying power of those who have lost jobs has been helped by Government relief payments, while the cash income (including Federal subsidies) of farmers for the first half-year was only 12 per cent below that of a year ago. According to estimates by the Department of Commerce, the total national income paid out, which represents the buying power of all the people, fell during first five months of this year less than 10 per cent below the corresponding period of 1937.

The maintenance of consumer incomes at levels high in relation to production has sustained consumption and facilitated the absorption of surplus goods, which is one of the conditions essential to recovery. With the good crops, a more favorable trend in employment, and the prospect of a heavy outpouring of Government funds, expectations of a further improvement in business conditions evidently are not unwarranted. Of course, as we observed a month ago, prosperity cannot be built upon consumer goods alone, nor can we go on indefinitely supporting business through the medium of Government credit. However, we repeat that a beginning has to be made somewhere, and once a trend has been established the cumulative effects tend to strengthen it.

Manifestly, the need is for conditions and policies that will promote capital investment, thus stimulating the capital goods industries which have been the most depressed. To achieve this an essential factor is confidence, especially confidence that the funds risked will run a fair chance of earning a reasonable return.

And, finally, a vital factor in the permanence of the recovery is the restoration of equitable

trading relations between the various segments of the economic system. There is ready recognition of the claim that the employing corporations shall pay the wage-workers a fair share of the value of the joint product, but there should be recognition also of the need for fair exchange relations between agriculture, transportation and the numerous branches of industry in which labor is employed. In the large sense the workers of all the industries are supplying each other with the necessaries and comforts they want for their homes. The workers, themselves, are the largest consumers, and "prosperity," including employment, depends upon right relations between them.

The post-war boom period developed many inequalities in trading relations, which eventually brought on the great depression; but between 1929 and 1935 many of these were ironed out by the mutual efforts of the industries to sell to each other. By the Fall of 1936 the industries were selling to each other on nearly a normal basis. Indeed in some lines demand exceeded the capacity of the industries, which had not been increased in the years of poor business, and prices were forced up by the competition of buyers rather than by the exactions of the industries, as commonly represented. The rapidity of the recovery in 1936 and the early months of 1937 caused an inevitable rise of costs, and this, together with the over-buying, prompted by excessive optimism, proved disastrous.

The recovery now under way is forced by the exhaustion of stocks, but its permanence depends upon the ability of the various groups of consumers to buy what each other has for sale. In other words, it depends upon another "ironing out" of trading relations, and the quickest and surest way is by ironing down the costs that are obstructing trade and causing unemployment. "Prosperity" is a state of rapidly flowing trade.

The Crop Outlook

The principal crops have made good progress during July, and the yields promise to be large on a per acre basis, but in the case of cotton and corn the acreages have been restricted under the A.A.A. program. The regions that suffered from drought in 1936 and preceding years have had ample rainfall thus far, and the only leading crops which are yet to be "made" are cotton and corn.

The wheat acreage was not restricted, as most of it is sown in the Fall and the 1938 Farm Act does not apply this year. According to the Government report of July 1, the acreage for harvest this year is 71,069,000, which compares with 64,460,000 last year, and 74,000,000 for the crop year 1918-19, the peak of the war-time expansion. The all-wheat crop this year is estimated by the crop-reporting bureau at 967,427,000 bushels, which is the second-largest on record. Including a carryover of about 200,000,000 bushels, the aggregate supply will afford at least 300,000,000 bushels for export, if the foreign demand exists. Inasmuch as the world crop is reported to be the largest on record, the prospect is that our carryover next year will be substantially increased.

The average acreage in corn over the ten years 1927-36 was 100,259,000 and in 1937 was reduced to 93,810,000. This year it is restricted to 92,146,000. The crop had a late start on account of rainy weather, but has done well in July. The official report estimates it at 2,482,000,000 bushels, compared with 2,644,975,000 in 1937. Consumption has been low, as the hog population is still nearly 25 per cent below the 1929-33 average. Hence the reduction in acreage. The corn-hog ratio is high, which means that farmers are feeding hogs to heavy weights.

The cotton crop has been reduced to a little less than 27,000,000 acres, from 34,400,000 acres last year. Reports from the belt vary from complaints of too much moisture to not enough, but with favorable weather for the finishing weeks, the yield should reach 11,500,000 bales and might go to 12,000,000.

The outlook for oats, barley, rye and the lesser field crops generally is good.

The price situation is less satisfactory than the crops. The large wheat crop in this country coincides with a record-breaking world crop. Although the new Farm Act was passed too late to restrict the wheat acreage, Congress provided that wheat-growers should be eligible to the loan privilege and "benefit" payments allowed to producers of the other crops named in the Act. As stated in these columns last month the minimum loan rate is fixed by law at 52 per cent of the parity price, which means the price at which the commodity should sell to give the producer an equal purchasing power to that of the producers of the goods which farmers buy. It was stated that this probably would work out a loan rate, on the average, of about 60 cents per bushel for wheat on farms. The Secretary of Agriculture announced the minimum rate on July 14, and the average is between 59 and 60 cents.

It should be understood that the borrower has the option of paying the loan and keeping the grain, or surrendering the grain in satisfaction of the loan. In fact, the farm loan rates at present are above the local market prices for wheat.

In announcing the loan rates the Secretary said that they had been fixed with consideration for the fact that the United States is naturally an exporter of wheat, and that it is desirable to preserve our foreign markets; in other words, it is desirable that our wheat surplus should move out of the country. Opinions expressed by the grain trade generally are to the

effect that so far as can be seen the Secretary has done as well as he could under the law, which requires that the minimum loan rate should be 52 per cent of the parity price.

The loan rates for corn and cotton on this year's crop have not yet been fixed. The "benefit" payments to farmers for cooperating in the program are 10 cents per bushel on wheat, 5 cents per bushel on corn and 2 cents per pound on cotton.

In view of the large prospective carryover, the Secretary of Agriculture has announced that plantings for the 1938-39 wheat crop will be restricted to 55,000,000 acres. When allowance is made for average abandonment, this is equivalent to a reduction of harvested acreage to about 45,000,000, which would be less than the pre-war average.

The Half Year's Profits

Financial statements for the second quarter and the half year published during the past month by leading corporations make an extremely uneven showing. Although the contraction of business activity was reflected, as had been expected, in a continued low level of profits generally, there was evidence on the part of numerous companies that operating expenses were under good control.

Reports of 275 manufacturing and merchandising corporations for the second quarter show combined net profits, less deficits, of approximately $101,000,000, compared with $91,000,000 for the same companies in the preceding quarter and with $351,000,000 in the second quarter of 1937. The decline of the second quarter from last year was 71.2 per cent, or slightly more than the drop of 67.5 per cent reported by a similar group of companies in the first quarter.

Reports for the first half year published to date by 335 corporations (including those which issue semi-annual but not quarterly statements) are given in the accompanying tabulation. These companies show combined net profits, less deficits, of $209,000,000, which compares with $682,000,000 for the same companies in the first half of last year and represents a decline of 69.3 per cent. Net worth of this group aggregated $10,354,000,000 on January 1, 1937, and $10,768,000,000 on January 1, 1938, upon which the half year's profits were at the *annual rates* of 13.2 per cent and 3.9 per cent, respectively.

As pointed out heretofore, the profits as published by a limited number of leading organizations indicate the trend of earnings, but do not provide an accurate measure of the average rate of earnings for industry as a whole. The latter can be found only in the Treasury Department "Statistics of Income," condensed summaries of which through 1935 were given in our issues of last March and April.

PROFITS OF LEADING INDUSTRIAL CORPORATIONS FOR THE FIRST HALF YEAR

Net Profits Are Shown After Depreciation, Interest, Taxes, and other Charges and Reserves, but Before Dividends.
Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.

(In Thousands of Dollars)

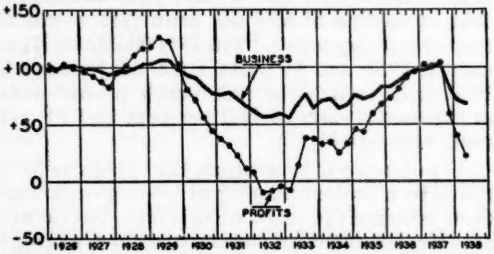
No.	Group	Net Profits Half Year 1937	Net Profits Half Year 1938	Per Cent Change	Net Worth January 1 1937	Net Worth January 1 1938	Per Cent Change	Annual Rate of Return % 1937	Annual Rate of Return % 1938
6	Amusements	$ 15,890	$ 10,043	—36.8	$196,342	$209,687	+ 6.8	16.2	9.6
1	Autos—General Motors	110,545	33,020	—70.1	970,843	992,305	+ 2.2	22.8	6.6
5	Autos—Others	33,124	126	—99.9	223,273	228,628	+ 2.4	29.7	0.1
19	Auto Equipment	14,677	D-1,858	....	117,703	124,769	+ 6.0	24.9	....
6	Baking	8,968	9,766	+ 8.9	250,085	248,803	— 0.5	7.2	7.8
13	Building Materials	13,243	3,428	—74.0	249,966	267,974	+ 7.2	10.6	2.5
18	Chemicals	82,829	37,087	—55.2	1,066,313	1,148,502	+ 7.7	15.5	6.4
9	Coal Mining	95	D-3,739	....	194,715	193,464	— 0.6	0.1	....
10	Electrical Equipment	46,835	20,315	—56.6	587,063	594,904	+ 1.3	15.9	6.8
18	Food Products—Misc.	42,212	36,784	—12.9	680,163	682,790	+ 0.4	12.4	10.8
11	Hardware and Tools	5,724	D-390	....	67,319	74,217	+10.2	17.0	....
8	Heating and Plumbing	4,680	D-1,031	....	70,391	76,316	+ 8.4	13.3	....
13	Household Goods and Sup.	5,552	907	—83.7	98,665	101,006	+ 2.4	11.2	1.8
1	Iron and Steel—U. S. Steel	64,735	D-6,303	....	1,564,517	1,592,212	+ 1.8	8.3	....
28	Iron and Steel—Others	68,600	D-1,290	....	1,288,034	1,400,544	+ 8.7	10.6	....
9	Liquors	4,166	4,233	+ 1.6	51,072	53,553	+ 5.0	16.3	15.8
20	Machinery	15,176	4,779	—68.5	140,107	153,252	+ 9.4	21.7	6.2
21	Merchandising	9,328	2,184	—76.6	220,293	228,785	+ 3.9	8.5	1.9
7	Mining, Non-ferrous	15,345*	8,697*	—43.3	161,791	164,861	+ 1.9	19.0	10.6
5	Office Equipment	6,292	2,592	—58.8	71,433	75,593	+ 5.8	17.6	6.9
9	Paper Products	5,643	2,393	—57.6	102,318	112,662	+10.1	11.0	4.2
14	Petroleum	47,800	33,111	—30.7	1,055,765	1,092,632	+ 3.5	9.1	6.1
8	Railway Equipment	12,498	D-116	....	184,696	191,104	+ 3.5	13.5	....
4	Shoes	4,612	717	—84.5	116,092	115,541	— 0.5	7.9	1.2
14	Textiles and Apparel	8,292	D-876	....	107,136	114,038	+ 6.4	15.5	....
45	Misc. Manufacturing	33,267	14,162	—57.4	382,032	397,212	+ 4.0	17.5	7.1
13	Misc. Services	1,655	244	—85.3	135,610	132,780	— 2.1	2.4	0.4
335	Total	$681.783	$208,985	—69.3	$10,353,737	$10,768,134	+ 4.0	13.2	3.9

D—Deficit. *—Before certain charges.

The Trend of Business and Profits

Earnings for the first half of 1938 declined less in the industries producing consumers goods — with certain exceptions — and more sharply in the heavy industries, where the drop in volume of business was much more severe. Deficits were reported by 35 per cent of the leading companies this year, against only 5 per cent last year.

About 85 per cent of the individual reports tabulated showed decreases in profits, or increases in deficits, for the first six months, but the remaining 15 per cent showed increases over last year. Gains were realized by some companies in such lines as baking, miscellaneous food products and petroleum.



Quarterly Index of Industrial Corporation Profits and The Annalist Index of Business Activity. (1936 = 100)

The longer-term trend of profits is shown on the chart which gives an index computed from rate of return of 200 leading industrial corporations, together with the Annalist index of business activity, both based on 1926 as 100 and adjusted for season variation. Figures for the latest quarter are preliminary.

Accompanying the sharp decline in business profits generally indicated by the figures of leading companies, Dun & Bradstreet reports that commercial failures of all types during the first half year were 44 per cent larger in number, and 66 per cent larger in liabilities, than in the corresponding period a year ago.

Sales figures are issued by a limited number of companies, and also show highly uneven changes this year. Aggregate sales of forty of the more important manufacturing companies, given in the accompanying list, declined from $2,928,000,000 to $2,131,000,000 or by 27.2 per cent, although there were a few individual increases. The trend of unfilled orders was also downward in most instances during the first half of this year.

A somewhat smaller decline in volume of business was registered by a group of chain store, department store and mail order houses, whose aggregate sales for the last year declined from $1,610,000,000 to $1,504,000,000, or by only 6.6 per cent.

% Change in Half Year's Sales, 1937-1938

Manufacturing		Merchandising	
Air Reduction Co.	—28.7	American Stores Co.	— 5.2
Allis-Chalmers Mfg.	+ 3.0	Barker Bros. Corp.	—17.6
Atlas Powder Co.	—17.4	Bond Stores	— 6.2
Baldwin Locomotive	+17.0	Chicago Mail Order	—12.4
Beatrice Creamery Co.	— 4.6	Consol. Retail Stores	— 6.5
Caterpillar Tractor	—36.6	Crown Drug	— 3.9
Certain-teed Products	—19.4	Edison Bros. Stores	+ 2.7
Chrysler Corporation	—54.1	Fanny Farmer Candy	+ 4.7
Cluett, Peabody	— 8.0	Grand Union Co.	— 2.4
Continental Steel	—49.2	W. T. Grant Co.	— 6.6
Douglas Aircraft	+95.8	H. L. Green Co.	—10.1
E. I. du Pont & Co.	—31.6	Interstate Dept. Stores	—21.8
Endicott-Johnson	—37.4	Jewel Tea Co.	+ 3.9
Fairbanks, Morse & Co.	—30.5	S. S. Kresge Co.	— 7.2
General Electric Co.	—23.5	S. H. Kress & Co.	— 6.4
General Foods Corp.	— 4.0	Kroger Groc. & Bak.	— 8.6
General Motors Corp.	—37.6	Lane Bryant, Inc.	—10.0
Hercules Powder Co.	—34.1	Lerner Stores Corp.	— 6.5
Inter. Shoe Corp.	—19.3	McCrory Stores Corp.	— 3.6
Johns-Manville Corp.	—24.9	McLellan Stores Corp.	— 6.7
Kimberly-Clark Corp.	— 4.2	Melville Shoe Corp.	— 8.0
Lone Star Cement	— 4.7	Montgomery Ward	— 6.4
Mead Corporation	—28.4	G. C. Murphy Co.	— 4.2
Minn.-Honeywell Reg.	—45.3	National Tea Co.	—12.1
Natl. Cash Register	— 8.7	Neisner Bros., Inc.	—13.4
Natl. Dairy Products	— 2.8	J. J. Newberry Co.	— 5.6
Natl. Lead Co.	—39.8	J. C. Penney Co.	— 8.7
Otis Elevator Co.	+17.8	Peoples Drug Stores	— 4.3
Phillips Petroleum	— 8.5	Reliable Stores Corp.	—29.6
Ruberoid Company	—28.4	Safeway Stores, Inc.	— 3.1
Sharon Steel	—66.3	Schiff Company	— 9.8
Shell Union Oil	— 1.3	Sears, Roebuck & Co.	—10.3
Simmons Company	—31.1	Spencer Shoe Corp.	—26.5
Standard Brands	—16.8	Spiegel, Inc.	—10.0
Sun Oil Co.	+1.0	Sterchi Brothers	—19.2
Tide Water Assoc. Oil	— 2.2	Sun Ray Drug Co.	+ 4.2
Union Oil Co.	— 0.3	Union Premier Food	+35.1
Wesson Oil & Snowdrift	— 9.8	Walgreen Company	— 1.4
Westinghouse Electric	—18.7	Western Auto Supply	— 5.8
Wheeling Steel Corp.	—40.4	F. W. Woolworth Co.	— 0.6

The Reduction of Inventories

While relatively few of the mid-year reports on corporate earnings have been accompanied by balance sheets, the available statements are of interest for the evidence they supply as to inventory changes.

A group of 70 leading companies, which to date have published balance sheets, showed total inventories on June 30, 1938 or thereabouts of approximately $605,000,000. This represented a decline from their inventory holdings on December 31, 1937 of $159,000,000 or 20.8 per cent, and a decline from those of June 30, 1937 of $111,000,000 or 15.5 per cent. Some of this reduction in dollar value, however, reflects merely the lower level of prices rather than changes in physical stocks.

Inventories of Leading Corporations on June 30, 1938, And Changes During the Six Months and Year

(In Thousands of Dollars)

No.	Manufacturing	Total June 30, 1938	Percentage Change During 6 Months	Percentage Change During Year
2	Aircraft	$ 11,997	—29.1	—23.1
4	Auto and Equipment	209,803	—39.1	—30.5
9	Building Materials	19,677	— 8.4	— 6.0
6	Chemicals	78,928	— 7.0	+ 4.9
4	Food Products—Misc.	31,148	+ 7.9	— 1.2
6	Household Goods	14,161	—12.1	—23.4
6	Machinery	25,676	—20.7	—17.2
5	Metals	28,821	— 8.8	— 6.3
1	Motion Picture	20,399	— 7.0	+ 7.3
2	Petroleum	60,993	+ 4.9	+ 8.1
3	Shoes	50,680	+ 1.8	—13.6
5	Textiles and Apparel	12,958	—10.0	— 7.1
13	Misc. Manufacturing	16,530	— 6.2	—13.7
66	Total Manufacturing	$581,771	—21.1	—15.4
	Merchandising			
4	Chain & Dept. Stores	23,719	—10.3	—18.0
70	Total	$605,490	—20.8	—15.5

About three-fourths of these individual companies had lower inventories on June 30, 1938 than at the year-end or the year previous. Where increases in inventories occurred, the amounts of increase were in most cases small.

Although the published corporate balance sheets provide only a small sampling, and do not measure the extent by which the reduction in stocks of finished goods may have been offset by new purchases of raw materials, the indicated downward trend of the totals conforms with numerous reports received from various trades. Department stores reporting to the Federal Reserve Board carried stocks 12 per cent less in dollar value on June 30th than a year previous.

Railroad and Utility Earnings Lower

The first half year was one of the most disastrous, from the standpoint of earnings, of any similar period in the history of American railroads. Preliminary figures for Class 1 systems indicate that total revenue from freight, passenger and other services declined by approximately $457,000,000, or 22 per cent. Operating expenses were reduced by $230,000,000, or 13 per cent, but net railway operating income dropped from $297,000,000 to $70,000,000. After payment of interest charges, but before any dividends, there was a *net deficit* of about $175,000,000, as against a *net income* of $36,000,000 last year.

A group of 25 leading utilities supplying electric, gas and other services, reporting for the twelve months ended June 30, had gross revenues practically equal to those of a year previous, but a decrease of 11 per cent in net income because of higher operating expenses and taxes.

The American Telephone & Telegraph Company and its principal telephone subsidiaries had total revenues for the six months ended May 31st slightly above those of a year previous. Taxes were 8 per cent higher, however, and other operating expenses 5 per cent higher, so that net income for the Bell System was 28 per cent below that of a year ago.

Dividend Declarations for First Half Year, 1937-38
(In Thousands of Dollars)

Group	1937	1938	% Chg.
Banks and insurance	$116,727	$119,826	+ 2.7
Chain stores	50,620	44,699	—11.7
Coppers	34,422	18,901	—45.1
Department stores	26,751	14,962	—44.1
Food and packing	94,780	82,902	—12.5
Mail order	13,432	13,492	+ 0.4
Motors	79,855	33,380	—58.2
Motor equipment	46,090	12,578	—72.7
Oils	188,664	177,132	— 6.1
Public utilities	483,449	429,000	—11.4
Railroads	115,581	83,872	—27.4
Railroad equipment	13,678	8,336	—38.7
Steels	76,309	27,750	—63.6
Tobacco	48,092	45,422	— 5.6
Miscellaneous	656,026	428,527	—34.7
Total	$2,044,477	$1,590,830	—22.2

Dividends 22% Below Last Year

Dividend declarations publicly reported, and compiled by the New York Times, show a decline of 22.2 per cent in dollar amount for the first six months, which was smaller than the rate of decline in corporate profits. Monthly figures, however, show that in January the dividends were 5.6 per cent *above* last year, but by June had fallen to 30.5 per cent *below*.

Money and Banking

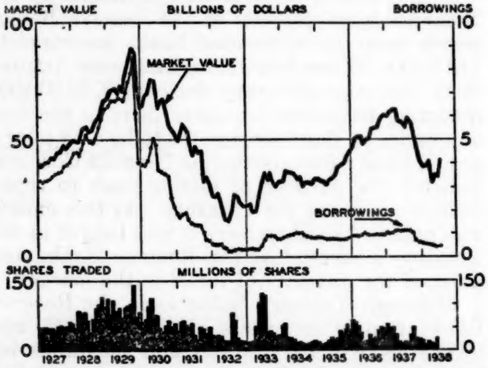
Owing chiefly to continued payments by the Treasury from deposits in the Reserve Banks, excess reserves of member banks increased to $3,150,000,000 on July 13, highest since August, 1936. Subsequently they declined $110,000,000 reflecting payments by subscribers to the first of a series of short-term notes to be sold over a period by the Reconstruction Finance Corporation for the purpose of raising cash to repay borrowings from the Treasury. As this money was paid in by subscribers it was lodged in the Treasury's account at the Reserve Banks and reduced the quantity of funds in the market.

Although Treasury balances in the Reserve Banks remain in excess of $700,000,000, and ultimately will be paid out and the funds incorporated in bank reserves, excess reserves may nevertheless have reached a peak for the time being. Cash redemptions of Treasury bills, which have been the principal source of additions to bank reserves heretofore, were suspended after July 20, and in the ensuing week the Treasury recommenced borrowing in excess of maturities. Should the Treasury fail to disburse promptly cash received in payment for bills or from subscriptions to R.F.C. notes, the effect might be to reduce excess reserves, or at least to limit their rise. Moreover, with the approach of Fall, seasonal currency requirements will be a factor in the situation. It should be stated, however, that excess reserves are expected to remain at abnormally high levels.

At the weekly reporting member banks, ordinary demand deposits (excluding government and interbank deposits) continued to rise and in the week of July 20 reached a new high since the middle of last year. Total earning assets, on the other hand, reached a new low for the year on the 13th but turned up sharply in the following week, due to a rise of investments in which subscriptions to new R.F.C. notes played a large part. Loans continued to decline and on the 20th were the lowest since early 1936.

Notwithstanding the rising prices and increasing volume of trading in the stock market, and larger offerings of new securities, reporting member bank loans to brokers and dealers declined during the first three weeks of July and on the 20th were only $45,000,000 above the May low point. This showing of

low credit demand in the stock market is paralleled by the report of the New York Stock Exchange as of July 1 revealing an increase of only $11,000,000 in total member borrowings during June. According to the Stock Exchange figures, the total on July 1 was $470,000,000, compared with $1,186,000,000 on September 1, last, and $8,549,000,000 at the all-time peak reached October 1, 1929. The accompanying diagram reflects the comparatively low total of credit employed in the stock market, not only at present, but throughout the period of the 1932-37 bull market.



New York Stock Exchange. Total Market Value of Listed Securities, Member Borrowings and Number of Shares Traded.

With excess reserves continuing to pile up, money rates in general remained little changed. Prices of Government securities were somewhat irregular but closed the month with a steady tone. As we go to press 90-day Treasury bills are quoted at 0.06 per cent, Treasury notes through December, 1939, on a no-yield basis, and the five-year notes at 0.80 per cent. In the corporate division, high grade issues were dull, but prices steady, with the real feature of the market the strength and activity of the lower grade rails.

New corporate financing in July, while less than in June, was substantial, amounting to about $150,000,000, according to preliminary tabulations. An encouraging feature of the recent offerings has been the increased proportion devoted to raising new capital. New issues of highest quality met with good reception.

The dollar was generally firm in terms of other currencies during July. Sterling declined from $4.95¾ to $4.91⅜ at the close of the month. Leading continental rates showed a tendency to move with sterling, with the exception of belgas which were steady. An important factor in the strength of the dollar is the continued heavy balance of merchandise trade running in favor of this country. While the value of both exports and general imports was smaller in June than in either May, 1938, or June, 1937, the trade balance was approximately $87,000,000 in our favor, compared with $21,000,000 against us in June last year. For the half year as a whole the United States accumulated a trade surplus of $631,000,000, the largest for any corresponding period since 1921, and an abrupt reversal of the results in the first half of 1937 when there was a trade deficit of $147,000,000. Naturally exchange rates have been affected.

Monetary gold stocks of the United States showed a further rise, and including imports of $36,000,000 (preliminary) during July plus domestic production, crossed the $13,000,000,000 mark for the first time. It is now estimated that the United States holds approximately 55 per cent of the total monetary gold stocks of all central banks and governments.

The World's Greatest Silver Hoard

Newspaper stories have told of the modern steel and concrete vault, with all latest appurtenances for the protection of treasure, recently completed on the grounds of the Military Academy at West Point; and of the contract for trucking about 35,000 short tons of silver bullion, about one-half of the Treasury's total silver stock, from New York City to the new storage place. The vault is 252 feet long, 166 feet wide, and 22 feet high. Further details are given in part as follows:

> Entrance to the vaults is by way of two sets of steel doors, between which is a loading platform for trucks. The three outer doors, through which the trucks will be driven with the metal, lift vertically, powered by an electric switch. The inner doors roll up and down, by electric impulse. The building is air conditioned. Within the inner doors is a lobby, and from this lobby a single steel door, drill-proof and flame-proof, leads into the vaults. There are observation turrets on the four corners of this massive cube. Floodlights and an elaborate system of electrical locks will add to the safety of the store within. The structure cost $529,000.

The Associated Press told of the trucking contract, as follows:

> Washington, June 30.—The Treasury hired Peter J. Malley of New York today to haul $1,290,000,000 worth of silver from New York to a new storehouse at West Point. He will be paid $157,000.
>
> Malley's trucks will be protected by fifty-five Coast Guardsmen on the fifty-mile trek. He will have to make the trip five days a week for nearly ten months to complete the job.

Mr. Malley said his plan was to run an average of 25 bus-type transportation trucks each day 5 days per week, and added:

> Each truck would carry about 350 bars of silver, weighing about 72 lbs. each, a total load of about eleven tons, having a statutory value of about $450,000 and a market value of about $150,000. Two Coast Guardsmen will ride on each truck. The danger of robbery was negligible, because robbers would find a truckload of bars a white elephant when it came to disposal.

The United States has so many problems that most of us forget the silver problem until it bobs up again. It bobbed up about 100 years ago, and again in 1878-1893—a fifteen-year period of silver-buying which was ended by President Cleveland. The country was in the

midst of panic when he called Congress together to stop the purchases, and it was done.

This ended silver purchases under the acts of 1878 and 1890. The aggregate of these purchases was approximately 459,949,000 ounces, and the cost was $464,210,000.

During the World War India's commercial exports became so large that means of payment were lacking and the United States sold its stock of silver dollars to England, which would have been fortunate, if the silver party in Congress had not insisted upon the Pittman Act, under which this silver was later replaced in Treasury vaults at a buying price of not less than $1.00 per ounce.

There the silver problem rested until the War inflation was followed by the world depression, when many people found themselves short of money, and called upon the Government for more; and more silver was proposed. It was urged that if the price of silver could be raised to $1.29 (former U. S. coinage rate) the purchasing power of China would be increased, our exports to China would be increased, bimetalism would be established, and prosperity would flow over the earth.

Silver Purchase Acts of 1933 and 1934

At a silver conference in London in 1933, under the leadership of the United States, eight nations made an agreement for holding or buying silver, the United States to buy not less than 24,412,410 ounces (the estimated amount of its own production). These purchases began in December, 1933, at 64.64 cents per ounce, the Government exacting 50 per cent of the coinage rate ($1.29) as "seignorage." The market price was about 43 cents.

This was only the beginning. Following the gold standard act of 1934, a bill passed the House for the purchase of "not less" than *fifty million ounces of silver monthly,* and was pending before the Senate. As a substitute measure the present law was enacted in June, 1934. Its principal provisions appear in Sections 2 and 3. Section 2 reads as follows:

> It is hereby declared to be the policy of the United States that the proportion of silver to gold in the monetary stocks of the United States should be increased, with the ultimate objective of having and maintaining, one-fourth of the monetary value of such stocks in silver.

Section 3 authorized and directed the Secretary of the Treasury to buy silver "at home or abroad" at such times and on such terms as "he may deem reasonable," but "not in excess of the monetary value" ($1.29), and only until the Treasury's silver holdings equalled 25 per cent of its combined gold and silver holdings. It was understood that the President did not favor the bill, but desired to move by means of international action. Senator Pittman so stated in offering the substitute and said that while he (the Senator) did not share the President's view he was willing to compromise.

This act, like the acts of 1878 and 1890, was passed in confidence that the proposed purchases would advance the market price of silver bullion to the coinage rate, and broaden the monetary use of the metal.

On August 9, 1934, the President issued a proclamation nationalizing silver, as gold had been nationalized earlier in the same year. Existing commercial stocks of silver were taken over by the Government at a fixed price, the Treasury claiming the difference between that and $1.29, as seignorage. Purchases abroad also began promptly. In August a shipment of 400 tons from London to New York was reported as the largest shipment of silver ever made across the Atlantic.

Effects of Treasury Purchases

During the depression silver had been falling in price, like other commodities. It had fallen from an average of 58 cents an ounce in 1928 to 27.8 cents in 1932. But in 1933, with the dollar off gold, and silver lifted by the eight-power agreement, silver averaged 34.7 cents. In 1934, with the aid of the United States Government, it averaged 47.9 cents. In the latter part of 1934, with the Treasury buying aggressively and the goal of $1.29 in view, speculation became very active.

However, instead of benefiting China and our trade with China, the rising price of silver had the opposite effect. Silver being the money, the rising price for the silver coins meant lower prices for the products of the country. Even in 1932 and 1933 the low prices for Chinese products had caused an adverse trade balance, with an outflow of both silver and gold. Now, Chinese traders were shipping silver direct to New York, to be sold to the United States Government.

The June, 1934, number of this publication, reviewing the silver situation and commenting upon the silver bill then pending in Congress, contained the following paragraph:

> As a measure of relief China may conclude to go to a depreciated paper basis, which would enable her to have any amount of money she wants and at a value to suit, and might provide a gold basis for the paper by selling her silver to the United States, if the price continues to rise here.

Within three months from the enactment of the law, the Minister of Finance of China addressed representations to the United States Government, of which the following is an extract:

> Since 1931 the rising of silver value in terms of foreign currency has involved severe deflation and economic losses to China and has dislocated China's balance of payments, in part at least by hampering exports. Recently the stimulation of silver prices abroad, to which exchange has not fully responded, has caused a serious drain of silver, creating great alarm.
>
> Silver exports of this year to date are over three times greater than any previous full year. Further material silver price increase would cause very serious injury to China, possibly severe panics. Although influential American circles advocate higher silver

prices, the Chinese Government, of course, makes no assumption concerning the American policy in this regard.

China is certain that the American Government desires to avoid any action that may aggravate present conditions, and therefore would appreciate an assurance that the American Government would refrain from any action that might cause a continuation of the present silver drain from China, and, accordingly, would cooperate to prevent further rise and to maintain the stability of silver which the London agreement contemplates. Indeed, from China's viewpoint, the stabilized level would be somewhat lower than the present price.

The National Government feels obliged actively to seek means of avoiding further hardships of silver fluctuation. It considers that China should not alone maintain the silver standard and is considering the gradual introduction of a gold basis currency, which will necessitate the acquiring of gold.

Since the American Government desires an increased proportion of silver in its monetary reserve, the National Government desires also to ascertain in principle whether the American Government is willing to exchange with the Chinese Government gold for silver.

In September, 1934, Mr. Li Ming, Chairman of the Bank of China, on business in New York, referring to the theory that the silver act would help the United States trade with China, made the following concise statement:

The theory that by raising the price of silver, China would be able to buy more in America, or America would be able to sell more to China, is not economically sound. America's purchasing power is not measured by the gold you possess, but is measured by the productivity of your national wealth. China, like every other country, pays for her imports chiefly by her exports. The silver in her possession, no matter how big that amount may be, does not help much in her purchases abroad. She will have to depend upon her exports and her exports alone.

These few sentences expose the fallacy of all "more money" plans for prosperity. The real purchasing power in the markets is not in "money" but, in the commodities and services being exchanged.

The text of the London Agreement, of which both China and the United States were signatories, proposed that "agreement be sought * * with a view to stabilizing the fluctuations in the price of silver," and the Chinese Government had signed it in the expectation of cooperation to this end.

In October, 1934, the Chinese Government placed an embargo on exports of silver, but as the world price continued to rise, smuggling developed on an important scale. Speculation was active, even running ahead of the Treasury bidding. In April, 1935, the London price reached 81 cents, with the Treasury paying 77½ cents for domestic silver.

In November, 1935, the Chinese Government took the final step of "nationalizing" silver, and providing for a managed paper currency. Meantime the London market had become top-heavy and was not supported by Washington. The price of foreign silver declined from 81 cents to 43 cents, delivered at New York, while the price of domestic silver was held at 77½ until January 3, 1938, when it was dropped to 64⅝, the present price.

China Abandons Silver

In May, 1936, the Chinese Government sought the aid of the United States in stabilizing its bank-note currency in relation to the monetary system of the United States, by purchases of silver from China. An agreement was entered upon by which the United States Government agreed to buy an unnamed amount of silver from the Chinese Government, giving dollar credits or gold for the same. This agreement has been renewed several times, and again within the last month.

This silver has come to this country from London, where it had been shipped, by way of Hong Kong, last year, and delivery has been made in New York. In the first six months of 1938 these receipts of Chinese coin amounted to about 140,000,000 ounces, of the value of $63,000,000, and since November have aggregated 190,000,000 ounces valued at $84,000,000. Total receipts of silver from China under the act of 1934 have been unofficially estimated at 300,000,000 ounces.

Although full information as to the proceeds of these purchases has not been made public, it is believed that aside from gold that has been earmarked, China's receipts have been expended or retained in the form of bank deposits.

Although these cash sales of Chinese coin in the United States began more than two years before the outbreak of the undeclared war with Japan, and have no relation to the War, they evidently have supplied the Chinese Government with a substantial fund available for expenditures abroad.

Operations Under the Silver Purchase Policy

The following table summarizes results under the silver purchase program since the authorization and direction of foreign purchases a little more than four years ago. It shows that when the law went into effect the Treasury held $7,856,000,000 of gold, and under the terms of the new act should have $2,619,000,000 of silver, valued at $1.29 per ounce, or 2,026,000,000 ounces. The total silver holdings, including subsidiary coins, were 693,000,000 ounces. The amount of silver to be acquired was 1,333,000,000 ounces. At the end of June, 1938, the amount of gold in reserves was $12,962,000,000, and after buying 1,687,000,000 ounces of silver, at a cost of about $900,000,000, the Treasury was still short 970,000,000 ounces of the required amount. The increasing gold stock has increased the amount of silver required.

Relative Holdings of Gold and Silver
(000,000s Omitted)

June 30,	1934	1935	1936	1937	1938
Gold Reserve ($)	7,856	9,115	10,608	12,318	12,962
Required Silver ($)	2,619	3,038	3,535	4,106	4,320
Required Silver (oz.)	2,026	2,350	2,735	3,176	3,341
Cumult. Acquisitions (oz.)	9	447	1,057	1,281	1,687
Silver in Treasury (oz.)	454	880	1,474	1,676	2,062
Silver in Subsid. Coin (oz.)	240	252	268	290	301
Total Stock (oz.)	698	1,132	1,742	1,966	2,371
To be Acquired (oz.)	1,883	1,318	993	1,210	970

The acquisitions include both domestic and foreign silver, but it is interesting to know that purchases of foreign silver aggregated 1,353,000,000 ounces, against 333,000,000 ounces acquired at home of which 220,000,000 ounces were newly mined.

The influence of the act of 1934 upon silver prices has been noted above. The influence of rising prices upon world silver production, and the influence of the silver purchase act upon the distribution of the metal, are shown by the following table of silver production, melted coin and United States Government purchases, in the five years 1934 - 1938, as follows:

(In Millions of Fine Ounces)

Year	World Silver Production United States	Foreign	Total	Demonetized Silver*	U.S. Treas. Acquis.
1934	33	157	190	258	306
1935	46	170	216	390	535
1936	63	188	251	304	333
1937	69	207	276	189	313
1938 (6 mos.)					201

*Received not only from China but from Indo-China, Spain, Mexico, South American countries, and others.

The total weight of silver coins from over the world melted down by the United States in the last four years has exceeded its purchases of newly-mined silver. For each ounce of newly-mined domestic silver, we bought 6.2 ounces of foreign silver. This is the net result of the effort to restore bimetalism throughout the world.

Other Results of the Policy

Among other results of this silver-purchasing policy may be noted:

1. That China, the one remaining country using silver as standard money, and formerly a net purchaser of approximately 100,000,000 ounces per year, has been driven to a managed currency, and is selling her age-old stocks of silver on the world market.

2. That the dream of reestablishing bimetalism has faded out forever. Although foreign speculators traded actively on the bull side of the market while the United States Government was clearly behind it, they stopped buying when the U. S. A. showed any sign of weakening. Not one of the other seven governments participating in the London Agreement even suggested renewal at its expiration, December 31, 1937. Purchases of their own silver production made by other parties to the agreement were finally dumped on the United States.

3. In its efforts to raise the price of silver, the United States was draining the world of existing stocks, and the price has been sustained only by the persistent buying of this country. The price dropped from 81 to 43 cents, because United States buying slackened, and is sustained at that price by United States buying.

4. The Treasury statement of July 1, 1938, shows an unexpended balance in the General Fund of $446,088,793 derived from "seignorage," on silver bullion acquired under the act of 1934, and on the asset side, 870,940,306 ounces of silver, valued at average cost, 55 cents per ounce, totalling $479,600,198. The latter entry is new, appearing July 1, for the first time. It shows silver upon which "seignorage" has not been made available for appropriation, and is a commendable innovation.

That this silver was not needed for our monetary stock is shown by the fact that in the first half of last year, one billion dollars of imported gold was bought and "sterilized" by the United States Government, to prevent its being used in the monetary system.

What of the Future?

Where do we go from here? The act of 1934 remains in force, silver production in the United States has increased from 24,000,000 ounces in 1932 to 69,000,000 ounces in 1937, world production increases as shown in above table, and most of it is sold to the United States Government. Silver importations in the first six months of this year have aggregated approximately 260,000,000 ounces and cost $112,000,000. Who is paying the bill, and what returns are the American people receiving on the investment? At no time after the purchasing campaign began could the United States have offered silver for sale without causing a panic, with a collapse of world prices, and this will continue to be so. The Treasury reports the cost of administering the silver purchase act (not including cost of silver) for the fiscal year 1937 as $287,000.

This review of the latest silver legislation and its results can be closed with no more appropriate comment than the following brief extract from the message of President Cleveland summoning the Congress of the United States to special session in 1893, and urging repeal of the silver-purchasing act of 1890. He said:

> The people of the United States are entitled to a sound and stable currency and to money recognized as such on every exchange and in every market of the world. Their government has no right to injure them by financial experiments opposed to the policy and practice of other civilized states, nor is it justified in permitting an exaggerated and unreasonable reliance on our material strength and ability to jeopardize the soundness of the people's money.

In the last session of Congress Senator Bailey or North Carolina offered a resolution directing that silver purchases should cease, but apparently it was not discussed.

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